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As I see

## EMERGENCY CREDIT AID FOR THE MORTGAGE MARKET

THE probability that housing starts next year will drop by 12.5 percent is causing considerable concern in some quarters. A recent article in the Wall Street Journal stated, "The present declining trend in private housing starts may prompt a bid in the next session of Congress to pump emergency credit into the mortgage money market, according to Rep. Albert Raines (D. - Ala.), chairman of the House Banking Committee's housing subcommittee." This action, in my opinion, would be neither justified nor wise.

If nonfarm housing starts slip by 12.5 percent to 1.2 million in 1960, as predicted by many economists, 1960 will still exceed 15 of the last 20 years. In only 3 years - 1950, 1955, and 1959 - has the number of new nonfarm dwelling units started, exceeded 1.3 million.

NEW NONFARM PUBLIC AND PRIVATE DWELLING UNITS STARTED
(Thousands of starts)

| Year | Starts | Year | Starts | Year | Starts | Year | Starts |
|---|---|---|---|---|---|---|---|
| 1940 | 603 | 1945 | 209 | 1950 | 1,396 | 1955 | 1,329 |
| 1941 | 706 | 1946 | 671 | 1951 | 1,091 | 1956 | 1,118 |
| 1942 | 356 | 1947 | 849 | 1952 | 1,127 | 1957 | 1,042 |
| 1943 | 191 | 1948 | 932 | 1953 | 1,104 | 1958 | 1,209 |
| 1944 | 142 | 1949 | 1,025 | 1954 | 1,220 | 1959 | 1,370* |

*Estimated.

If the value of new construction of all types remains about the same, 1960 will be the second best year for the construction industry, as a whole, according to this measure of total construction activity. Although the amount of residential construction is expected to decline slightly in 1960, the increase in other construction is expected to be great enough to make total construction activity about the same in 1960 as in 1959. Thus, 1959 and 1960 would be the first and second best years on record, since 1959 was the first year that value of construction passed $35.5 billion in 1947-49 dollars.

## VALUE OF NEW PRIVATE AND PUBLIC CONSTRUCTION PUT IN PLACE IN 1947-49 PRICES
(Millions of dollars)

| Year | Value | Year | Value | Year | Value | Year | Value |
|---|---|---|---|---|---|---|---|
| 1940 | $16,767 | 1945 | $ 8,681 | 1950 | $27,972 | 1955 | $35,334 |
| 1941 | 21,714 | 1946 | 16,346 | 1951 | 28,289 | 1956 | 34,681 |
| 1942 | 22,852 | 1947 | 19,070 | 1952 | 29,051 | 1957 | 34,944 |
| 1943 | 12,812 | 1948 | 22,259 | 1953 | 30,375 | 1958 | 35,495 |
| 1944 | 8,174 | 1949 | 23,544 | 1954 | 32,395 | 1959 | 38,800* |

*Estimated.

The mortgage market has absorbed an average of 34 percent of all the funds flowing through financial institutions, pension funds, and individual accounts from 1950 to 1958. These financial institutions include all banks, savings banks, savings and loan associations, life insurance companies, etc. In 1956, 48 percent of the net flow into capital and equity instruments went to mortgages.

## FLOW OF FUNDS INTO CAPITAL AND EQUITY MARKETS
(Billions of dollars)

| Year | Net Total Capital and Equity* Market Flow | Net Mortgage Flow | Mortgages As a Percent of Total |
|---|---|---|---|
| 1950 | $40.1 | $10.1 | 25% |
| 1951 | 28.6 | 9.5 | 33 |
| 1952 | 38.1 | 9.1 | 24 |
| 1953 | 29.8 | 9.9 | 33 |
| 1954 | 28.4 | 12.5 | 44 |
| 1955 | 43.8 | 16.2 | 37 |
| 1956 | 30.6 | 14.6 | 48 |
| 1957 | 36.7 | 12.1 | 33 |
| 1958 | 45.4 | 14.6 | 32 |
| Ave. 1950-58 | 35.7 | 12.1 | 34 |

*Federal obligations, State and local obligations, corporate and foreign bonds, corporate stock, mortgages, consumer credit, security credit, and other loans.

In a nutshell, the problem, as I see it, is this:

1. Is it necessary that every year set new records in construction regardless of the effects on the economy?

2. Should a larger percentage of the savings of the American people be diverted to construction and, if so, how is this diversion to be accomplished?

3. Should Fannie Mae buy mortgages at par in order to hold down interest rates in the home mortgage field?

4. Should the Federal Government, through the Treasury Department and the Federal Reserve Board, increase money and credit through selling bonds to the banks?

My own answer to each of these questions would be a resounding no. I see no reason, for instance, why each succeeding year, regardless of other factors, must necessarily set a new record in either the total number of new dwelling units produced or in the total dollar volume of all construction. It is inherent in our free enterprise system that production of any product will respond to fluctuations in demand in relationship to cost. In a democracy we can never achieve stability with all years at the peak. Some years we will overbuild and in those years the surplus will be hard to move. In other years we will underbuild and houses will disappear from the market as rapidly as they can be produced. There is no more reason why the Government should undertake to insure a new peak in construction each year than there is that it should guarantee to the automobile manufacturers that each year they could produce and sell a larger number of automobiles than during the preceding year. We should have learned, from our sorry experience in the agricultural field, that booming production often results in toppling inventories which eventually depress prices, in spite of all attempts to maintain them. In many ways the agricultural field is in much worse shape today than it has been for many years, in spite of the many billions of dollars of the taxpayers' money spent in an effort to stabilize the market.

A statement by Saul B. Klaman, in a paper presented to the Senate subcommittee studying mortgage credit, is pertinent at this point. "While increased and improved housing facilities for all of our citizens should be among our Nation's leading goals, of importance also are provisions for expanded and improved educational facilities, health centers, roads and highways, plant facilities, and national defenses." When the Government begins to shift the allocation of funds as determined by the market place from one use to another, it is automatically involved in setting priorities on all the uses of funds. The price mechanism can allocate the capital funds into those uses which will bring the greatest return. Why should this impartial system be deposed for a system of political favoritism?

Believing as I do, in a free economy with a minimum of Government interference, I firmly believe that the percentage of the savings of the American public that goes into construction, must necessarily be determined by the competitive factors in the market. One of our great difficulties in the United States during the past 30 years has been that we bought things we didn't need with money we didn't have. There are two logical reasons why this has taken place. The first has been that the rewards for saving have been too small. Interest rates have been held at a very low level, and the small amount of interest received was subject to still further diminution by high tax rates. The second factor responsible has been, that during this entire period inflation was cutting constantly into the purchasing power of the dollar. A dollar spent today will buy much more than $1.03 a year from now. Each succeeding year that

purchases were deferred in an attempt to build up capital, inflation decreased the value of the savings faster than they were increased by accrued interest. From the standpoint of receiving the maximum purchasing power from the money spent, the spendthrift, in a period of inflation, who spends each dollar as he receives it, actually secures more goods and services than the thrifty individual who saves his earnings, only to find that those earnings, plus accrued interest, will buy less than his income would have bought had he spent it as received. If we do not increase our savings and are going to spend more on housing, we must continue to inflate or we must divert from highways, schools, defense, and other legitimate claims on the savings of the American people, funds which would otherwise be spent in these fields. There is no way to make this diversion other than by mortgage borrowers' being willing to pay as much or more for the use of the money as the competitive uses will pay. Actually, however, the higher interest rate and the opinion that inflation has been stopped will create more savings and will, accordingly, increase the amount of money available, not only for housing, but for other necessary projects.

I believe the management of Fannie Mae has been good and I think that, left to its own devices, a secondary mortgage market of the type originally set up is very helpful. Unfortunately, however, Congress from time to time uses Fannie Mae, not as a legitimate secondary mortgage market, but as an instrument to pump Government funds into the housing field at interest rates much below those set by market factors. When Fannie Mae is given a billion dollars by Congress and told to buy certain mortgages at par, which would ordinarily sell for 95-96, the taxpayers are subsidizing the builder and the purchaser of homes. Not only that, but the increased borrowing, which results with the creation of additional credit has a strong inflationary effect on the price level and on the purchasing power of money.

The only other way that housing could be stimulated would be for the Federal Reserve Board and the Treasury Department of the Federal Government to reverse the tight money policy. This could be done by selling short-term Government bonds to the banks, which would be equivalent to printing greenbacks. It is a policy that was followed consistently for several decades, and if continued would result, first, in more rapid price rises than we have had in the past; second, in a more rapid loss of foreign markets than we have experienced thus far, as we would price ourselves out of world markets rapidly; and, third, in a great increase in imports, as foreign manufacturers would be able to underbid American manufacturers in our own home markets. This would bring on unemployment in America of sizable amounts, and might be deferred temporarily by a revaluation of our currency.

We can live with a temporary drop in housing starts better than we can live with its alternatives.

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